

**Internal Revenue Service**

Department of the Treasury  
Washington, DC 20224

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Date:

July 30, 2021

**LEGEND:**

Taxpayer: =

Master Fund =

Individual =

Manager =

Manager GP =

Fund GP =

Partnership X =

Fund Y =

State =

Country =

a =

b =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Date 6 =

Date 7 =

Date 8 =

Date 9 =

Date 10 =

Date 11 =

Year 1 =

Year 2 =

Year 3 =

Year 4 =

Dear :

This letter responds to a request for a private letter ruling that Taxpayer filed with the Internal Revenue Service (Service). Taxpayer's letter requested an extension of time under § 301.9100 of the Procedure and Administration Regulations ("the Regulations") to make an election to use the mark-to-market method of accounting under § 475(f)(1) of the Internal Revenue Code ("the Code"), effective for the taxable year that ended Date 1. Taxpayer requested relief on Date 2.

### **FACTS**

On Date 3, Individual formed Taxpayer, a State limited partnership. Taxpayer was a limited partner of Master Fund, a Country exempted limited partnership.

Individual formed Fund GP, a State limited liability company. Fund GP was the general partner of Taxpayer and Master Fund. Individual was admitted as the managing member of Fund GP. Fund GP was entitled to an allocation of profits from Taxpayer and Master Fund.

Individual formed Manager GP, a State limited liability company, and Manager, a State limited partnership. Individual was also a managing member of Manager GP. Manager GP was a general partner of Manager. Manager was paid a fee by Taxpayer and Master Fund for investment management services.

Taxpayer represents that ultimately most of the Year 1 allocable items of the Taxpayer and Master Fund, and all the Year 1 allocable items of Manager were included in the taxable income of Individual.

Taxpayer began trading securities on Date 4. Taxpayer conducted its trading activities through Master Fund from Date 4 until Master Fund ceased all trading activity in Date 5. Master Fund was dissolved later in Year 1. Taxpayer continued trading activities directly until Date 6, when Taxpayer ceased all trading activity. Taxpayer sustained annual net losses in each year of its existence. Taxpayer represents that it qualified as a trader in securities for federal income tax purposes from Date 7 through Date 6.

Partnership X is a State limited partnership that sponsors Fund Y, a State limited partnership. Taxpayer represents that Individual entered into negotiations with Partnership X for Partnership X to engage Manager to perform sub-advisory services for the portion of Fund Y's investment program that aligned with Taxpayer's investment strategy. These negotiations resulted in the execution of a Sub-Advisory Agreement ("the Agreement") on Date 8. The Agreement provided that for federal income tax purposes, Manager would be treated as a partner of Fund Y. The Agreement, however, did not expressly address the tax character of Manager's share of Fund Y's profits. Taxpayer represents that based on conversations with Partnership X, Individual's understanding was that the character of Manager's allocable share of Fund Y's profits would be capital gain.

The Schedule K-1 for Year 1 was issued to Manager on Date 9. The Schedule K-1 showed that Manager had been allocated a share of Fund Y's profits, and that the entire allocation was characterized as ordinary income. Taxpayer represents that the ordinary character was because Fund Y had made an election under § 475(f)(1) of the Code to use the mark-to-market method of accounting, effective for the taxable year that ended Date 1. Taxpayer represents that this was the first time that Individual became aware of the existence of a § 475(f)(1) election. Taxpayer represents that Partnership X never mentioned, provided written information about, or otherwise discussed the possibility of Fund Y making an election under § 475(f)(1). Manager timely filed its extended federal income tax return for Year 1 based on the Schedule K-1

that Manager received from Partnership X. Taxpayer represents that in late Year 2, Manager terminated its relationship with Partnership X and Manager ceased operations.

Taxpayer represents that Individual would have caused Taxpayer to have made a timely election under § 475(f)(1) for Year 1 if Individual had known that Fund Y had made the election for Year 1. If Taxpayer had made a timely election under § 475(f)(1) for Year 1, the election would have been due on Date 10, the due date of Taxpayer's Year 3 federal income tax return (without regard to any extension).

In Date 11, during the process of preparing Manager's Year 2 federal income tax return, Individual became aware of the process to request an extension of time under § 301.9100 of the Regulations to seek relief to make a late § 475(f)(1) election. Individual subsequently met with counsel to discuss the matter, and then on Date 2 requested a private letter ruling on behalf of Taxpayer seeking an extension of time under § 301.9100 to make a § 475(f)(1) election effective for the taxable year that ended Date 1.

### **LAW AND ANALYSIS**

Taxpayer is not entitled to relief under § 301.9100 to make a late § 475(f)(1) election because Taxpayer did not act reasonably and in good faith, and granting relief would prejudice the interests of the Government.

#### **Relief under § 301.9100 to make a late § 475(f)(1) election is denied**

Section 475(f)(1) provides that a taxpayer engaged in a trade or business as a trader in securities may elect to apply the mark-to-market method of accounting to securities held in connection with such trade or business. Section 7805(d) provides that, except to the extent otherwise provided by the Code, any election shall be made at such time and in such manner as the Secretary shall prescribe.

Rev. Proc. 99-17, 1999-1 C.B. 503, sets forth the requirements for making an election under § 475(f). Under section 5.03 of that revenue procedure, a taxpayer must file an election statement not later than the due date (without regard to any extension) of the original federal income tax return for the taxable year immediately preceding the election year and must attach the statement either to that return or, if applicable, to a request for an extension of time to file that return. Section 5.04 of Rev. Proc. 99-17 sets forth the requirements for the statement. The statement must describe the election being made, the first taxable year for which the election is effective, and, in the case of an election under § 475(f), the trade or business for which the election is made. Section 4 of Rev. Proc. 99-17 provides that an election under § 475(f) determines the method of accounting that an electing taxpayer is required to use for federal income tax purposes for securities subject to the election. Once a valid election is made, the taxpayer is required to use a mark-to-market method of accounting under § 475. Section 4 of Rev. Proc. 99-17 also provides that if a taxpayer fails to change the taxpayer's method of

accounting to comply with the election, then the taxpayer is on an impermissible method.

Section 6.01 of Rev. Proc. 99-17<sup>1</sup> provides that a change in a taxpayer's method of accounting is a change in method of accounting to which the provisions of § 446 and § 481 and the regulations promulgated thereunder apply. Section 6.03 of Rev. Proc. 99-17 generally provides that if a taxpayer changes its method of accounting under section 6.01 of Rev. Proc. 99-17, the taxpayer must take into account the net amount of the § 481(a) adjustment over the applicable period.

Section 23.01 of Rev. Proc. 2017-30, 2017-18 I.R.B. 1131, provides procedures for a trader in securities that has made a § 475(f)(1) election to obtain automatic consent of the Commissioner to change the trader's method of accounting for securities to use the mark-to-market method of accounting under § 475.<sup>2</sup> Section 23.01(4) of Rev. Proc. 2017-30 refers to section 5 of Rev. Proc. 99-17 for the requirements to make a § 475(f)(1) election.

Rev. Proc. 2015-13, 2015-5 I.R.B. 419, sets forth the general procedures under § 446(e) to obtain the consent of the Commissioner to change a method of accounting for federal income tax purposes, including the procedures to obtain the automatic consent of the Commissioner to change a method of accounting in Rev. Proc. 2017-30. Under section 7.02 of Rev. Proc. 2015-13, unless otherwise provided in a specific change listed in Rev. Proc. 2017-30, a taxpayer making a change in method of accounting must apply § 481(a) and take into account the § 481(a) adjustment in the manner provided in section 7.03 of Rev. Proc. 2015-13. Section 23.01 of Rev. Proc. 2017-30 does not contain an exception to the rule in section 7.02 of Rev. Proc. 2015-13.

Section 301.9100-1(c) provides, in part, that the Commissioner has discretion to grant a reasonable extension of time to make a regulatory election (defined in § 301.9100-1(b) as an election whose due date is prescribed by regulations published in the Federal Register, or by a revenue ruling, revenue procedure, notice, or announcement published in the Internal Revenue Bulletin). Section 301.9100-1(b) defines the term election to include a request to change an accounting method.

Section 301.9100-3 sets forth rules that the Commissioner must use to determine whether it will grant an extension of time for regulatory elections that do not meet the requirements of § 301.9100-2 for an automatic extension. Generally, a taxpayer must provide sufficient evidence to establish to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith, and that the grant of relief will not prejudice the interests of the Government.

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<sup>1</sup> Section 6 of Rev. Proc. 99-17 was superseded by Rev. Proc. 99-49, 1999-2 C.B. 725.

<sup>2</sup> Rev. Proc. 2017-30 is the automatic method change revenue procedure that would have applied to Taxpayer's election filing, had it been timely filed.

Except as provided in § 301.9100-3(b)(3), § 301.9100-3(b)(1) provides rules for determining when a taxpayer is deemed to have acted reasonably and in good faith. Section 301.9100-3(b)(1)(i) provides that a taxpayer will be deemed to have acted reasonably and in good faith if the taxpayer requests relief under § 301.9100-3 before the failure to make the regulatory election is discovered by the Service. Section 301.9100-3(b)(3) provides rules as to when a taxpayer is deemed to have not acted reasonably and in good faith. Section 301.9100-3(b)(3)(iii) provides that a taxpayer is deemed to have not acted reasonably and in good faith if specific facts have changed since the due date for making the election that make the election advantageous to a taxpayer. In such a case, the Service will grant relief only when the taxpayer provides strong proof that the taxpayer's decision to seek relief did not involve hindsight.

Section 301.9100-3(c) provides that the Commissioner will grant a reasonable extension of time to make a regulatory election only when the interests of the Government will not be prejudiced by the granting of relief. Section 301.9100-3(c)(1)(i) provides that the interests of the Government are prejudiced if granting relief would result in a taxpayer having a lower tax liability in the aggregate for all taxable years affected by the election than the taxpayer would have had if the election had been timely made (taking into account the time value of money).

Section 301.9100-3(c)(2) provides special rules for accounting method regulatory elections. Section 301.9100-3(c)(2)(ii) provides that the interests of the Government are deemed to be prejudiced except in unusual and compelling circumstances if the accounting method regulatory election for which relief is requested requires an adjustment under § 481(a) (or would require an adjustment under § 481(a) if the taxpayer changed to the method of accounting for which relief is requested in a taxable year subsequent to the taxable year the election should have been made).

#### **(a) Taxpayer did not act reasonably and in good faith**

Section 301.9100-3(b)(3)(iii) provides that a taxpayer is deemed to have not acted reasonably and in good faith if specific facts have changed since the due date for making the election that make the election advantageous to a taxpayer. In such a case, the Service will grant relief only when the taxpayer provides strong proof that the taxpayer's decision to seek relief did not involve hindsight.

To make a timely § 475(f)(1) election for the taxable year that ended Date 1, Taxpayer would have had to make the election by Date 10, the due date of Taxpayer's Year 3 federal income tax return (without regard to any extension). Taxpayer's request for a late filing of the § 475(f)(1) election was not made until Date 2, which provided Taxpayer the benefit of nearly a months of hindsight. Taxpayer continued to trade securities until Date 6, which was approximately b months after the Date 10 due date for making the § 475(f)(1) election. Accordingly, Taxpayer gained a benefit from hindsight because Taxpayer was able to determine the effect of a § 475(f)(1) election with the benefit of knowing Taxpayer's trading results for Year 1.

Additionally, Manager received a Schedule K-1 on Date 9, showing Manager's allocable share and tax character of Fund Y's Year 1 trading profits before Taxpayer filed in Year 4 a request for relief under § 301.9100-3 to make a late § 475(f)(1) election. Taxpayer gained a benefit from hindsight because Taxpayer was able to determine the effect of a § 475(f)(1) election with the benefit of knowing Manager's allocable share and tax character of profits from Fund Y for Year 1. Moreover, Taxpayer did not provide strong proof showing that its decision to seek relief to make a late election did not involve hindsight. Accordingly, under § 301.9100-3(b)(3), Taxpayer is deemed to have not acted reasonably and in good faith.

### **(b) Granting Relief Would Prejudice the Interests of the Government**

Under § 301.9100-3(c)(2)(ii), the interests of the Government are deemed to be prejudiced, except in unusual and compelling circumstances, if the accounting method regulatory election for which relief is requested requires an adjustment under § 481(a) (or would require an adjustment under § 481(a) if the taxpayer changed to the method of accounting for which relief is requested in a taxable year subsequent to the taxable year the election should have been made). Taxpayer has not presented unusual and compelling circumstances for its failure to timely make a § 475(f)(1) election.

Since a § 475(f)(1) election is an accounting method regulatory election that requires a § 481(a) adjustment, the interests of the Government are deemed to be prejudiced because Taxpayer has failed to present unusual and compelling circumstances to justify granting the requested relief.

### **CONCLUSION**

Based on the facts and representations submitted, we conclude that Taxpayer has not satisfied the requirements to justify granting an extension of time under § 301.9100-3 to make an election under § 475(f)(1) to use the mark-to-market method of accounting effective for the taxable year that ended Date 1. Specifically, Taxpayer has failed to demonstrate that Taxpayer acted reasonably and in good faith, and that granting relief will not prejudice the interests of the Government. Accordingly, Taxpayer's request for an extension of time to make an election under § 475(f)(1) for the taxable year that ended Date 1 is denied.

Except as expressly provided herein, no opinion is expressed or implied concerning the federal income tax consequences of the transactions described above. In particular, no opinion is expressed or implied as to whether Taxpayer's securities trading activities constitute those of a trader in securities eligible to make the mark-to-market election under § 475(f)(1).

This ruling is directed only to the taxpayer that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the terms of a power of attorney on file in this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

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K. Scott Brown  
Branch Chief, Branch 3  
Office of the Associate Chief Counsel  
(Financial Institutions & Products)

Enclosures:

Copy of this letter  
Copy for section 6110 purposes

cc: